UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF FLORIDA

In Re	)	
	)	In Bankruptcy
HOWARD FRIEDMAN	)	
VIVIAN FRIEDMAN	)	Case No. 99-20856
	)	
Debtors.	)	
_____	)	
	)	
LATIN AMERICAN CASINOS, INC., d/b/a REPOSSESSION AUCTION, INC., a Florida corporation,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Adversary No. 99-2166-BKC-RBR-A
	)	
HOWARD FRIEDMAN and VIVIAN FRIEDMAN,	)	
	)	
Defendants.	)	

O P I N I O N

The issue before the Court is whether a debt is nondischargeable pursuant to 11 U.S.C. §§ 523(a)(2)(A) and (a)(6).

The Plaintiff, Latin American Casinos, Inc., d/b/a Repossession Auction, Inc. ("Repossession") was in the business of selling used automobiles from 1991 to 1995 in Miami. Lloyd Lyons, who is now deceased, was the CEO of Repossession, and his wife, Geraldine Lyons, was the Corporate Secretary for Repossession. The Lyons' son-in-law, Jeffrey Felder, was the President of Repossession. In 1995, Repossession decided to change the nature of its business from the sale of used cars to the leasing of slot machines in Latin America based on Mr. Lyon's belief that

Repossession would earn more money in the slot machine business than in the used car business.

The Defendants, Howard and Vivian Friedman, started a business known as Ideal Motors in April, 1993. The business sold cars and other vehicles from a lot in Pompano Beach. In addition, Mr. Friedman was also working as a buyer for Repossession. His function was to purchase used cars for Repossession at auctions around the country. He used cards which identified him as an authorized agent of Repossession to purchase cars with Repossession checks for amounts that were approved by Repossession. The cars were titled in the name of Repossession and delivered to Repossession's lot in Miami. Mr. Friedman was paid a commission of $75 for each car purchased.

In the spring of 1994, Mr. Lyons approached Mr. Friedman and Mr. Felder about operating Repossession's car sales business with each of the parties putting up $25,000. Mr. Felder turned down the offer, but Mr. Friedman decided to accept it based upon Mr. Lyon's representation that the business was extremely profitable. According to Mr. Lyons, Repossession made over $1,000,000 selling used cars in at least one year of its existence. However, neither Mr. nor Mrs. Friedman was shown the books or tax records of Repossession.

In April, 1994, the Friedmans moved their business, Ideal Motors, from Pompano Beach to the Miami location of Repossession. At this time, the Friedmans incorporated V.R.K. Inc., which would do business as Ideal Motors. The Friedmans invested $50,000 in their business.

In May, 1994, Repossession and the Friedmans entered into several agreements to memorialize the transaction. The Floor Plan and Security Agreement and Revolving Promissory Note provided that Repossession would supply Mr. Friedman and his corporation with a $500,000 credit line which Mr. Friedman could use to purchase cars at auctions throughout the country. The Floor Plan Agreement provided that payment for the financed vehicles was payable within 90 days of the sale of the vehicle or upon demand, whichever was sooner. Pursuant to the terms of the Agreement, Ideal gave Repossession a first priority security interest in the following collateral: (i) accounts and accounts receivable; (ii) inventory; (iii) equipment; (iv) general intangibles; (v) documents of title; (vi) chattel paper; and (vii) instruments. This collateral constituted virtually all of Ideal's assets, both at the time that the Floor Plan Agreement was executed and at the time of default.

In practice, no money was ever advanced directly to the Friedmans or their corporation. Mr. Friedman continued to use the same auction cards of Repossession to attend automobile auctions. Mr. Friedman purchased the vehicles with Repossession checks, and the vehicles were titled in the name of Repossession. The vehicles were shipped from the auctions to the lot which was shared by Repossession and Ideal for sale by Ideal. The cars remained titled in the name of Repossession until they were sold and title transferred to the purchaser. For each car sold, Ideal was required to repay Repossession the original purchase price of the vehicle plus interest plus a flat fee per vehicle.

Ideal paid rent on the lot of $6,000 per month to

Repossession. The rent was current through April, 1995. Repossession continued to occupy the same office facility as Ideal, and Ideal paid for the electricity used by both Repossession and Ideal. In addition, Ideal paid the costs of running the business. These costs included commissions to the salesmen, telephone, advertising, car repairs, and salaries. Mr. Friedman's salary was $400 per week, and Mrs. Friedman's salary was $500 per week, but there were several months when neither one of them drew their salary.

The business did not flourish. In many instances, Repossession determined the selling price of the vehicle, and the price did not allow Ideal to make sufficient profit to cover its costs. Further, Mr. Lyons cut back on the number and location of auctions which Mr. Friedman could attend. Mr. Friedman was unable to acquire the new and appropriate vehicles that he needed to keep customers coming back to the lot.

Mr. Friedman told Mr. Felder on two occasions prior to April, 1995, that the business was in trouble. Mr. Felder referred Mr. Friedman to Mr. Lyons. Mr. Friedman testified that he called Mr. Lyons three times to explain that the business was in trouble, but Mr. Lyons would not discuss it, used language which Mr. Friedman would not repeat, told him not to call him again, and hung up on him on each of the three occasions.

During the period from May 1, 1994, through April 18, 1995, Ideal paid over $1,500,000 to Repossession for automobiles, rent, interest, and other costs.

Repossession, through Mr. Felder, took monthly inventory of

all vehicles on Ideal's lot. Everything was fine until April 29, 1995, when Mr. Felder's inventory disclosed that 20 vehicles which were supposed to be on Ideal's lot could not be accounted for. Mr. Felder immediately reported the situation to Mr. Lyons, and Mr. Lyons confronted Mr. Friedman about the inventory shortfall. A physical altercation ensued wherein Mr. Lyons beat up Mr. Friedman. The police were called, and Mr. Friedman left with a bloody nose. Neither Mr. nor Mrs. Friedman returned to the lot.

The Friedmans took their salary once or twice in May, 1995, They also paid cellular phone bills and Mrs. Friedman's car payment.

After Ideal vacated the lot, Ideal customers approached Repossession concerning the whereabouts of their titles. Repossession processed the titles even though it had not been paid for the vehicles.

The Friedmans filed a petition pursuant to Chapter 7 of the Bankruptcy Code in 1999. Repossession filed an adversary proceeding against the Friedmans pursuant to 11 U.S.C. § 523(a)(2)(A) and (6). A trial was held on April 17, 2000, and the parties have submitted post-trial findings of fact and conclusions of law.

11 U.S.C. §523(a) provides in pertinent part as follows:

> (a) A discharge under section 727. . . of this title does not discharge an individual debtor from any debt --
>
> . . . .
>
> (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by --

> (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;
>
> . . . .
>
> (6) for willful and malicious injury by the debtor to another entity or to the property of another entity(.)

The party seeking to establish an exception to the discharge bears the burden of proof. In re Harasymiw, 895 F.2d 1170, 1172 (7th Cir. 1990). The burden of proof required to establish an exception to discharge is a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 291 (1991). To further the policy of providing a debtor with a fresh start in bankruptcy, "exceptions to discharge are to be construed strictly against a creditor and liberally in favor of a debtor." In re Scarlata, 979 F.2d 521, 524 (7th Cir. 1992).

In order to successfully bring an action under §523(a)(2)(A), a creditor must prove that the debtor committed "actual fraud". Field v. Mans, 516 U.S. 59, 69 (1995). To prove "actual fraud", a creditor must establish the following common law elements of fraud: (1) the debtor made a false representation; (2) the debtor knew that the representation was false at the time that he made it; (3) the debtor made the representation with the intention and purpose of deceiving the creditor; (4) the creditor justifiably relied on the representation; and (5) the creditor sustained a loss as the proximate result of the representation. In re Chinchilla, 202 B.R. 1010, 1013-14 (Bankr. S.D. Fla. 1996).

Neither Mr. Felder nor Mr. Lyons could remember any misrepresentations made by Mrs. Friedman. Mrs. Friedman stated that she was afraid of Mr. Lyons and did not talk to him about any matter. Mrs. Friedman did not make any representations to Repossession or any of its employees regarding payment to be made by Ideal to Repossession. She did not sell vehicles to the general public or take money from the buyers.

The Friedmans clearly did not intend to defraud Repossession when the agreements were entered into in May, 1994. The Friedmans closed down their Pompano Beach facility and moved their operation to Repossession's lot in Miami. They put $50,000 of their own money into the business. They worked long hours for modest salaries and often without their paychecks. They paid over $1,000,000 to Repossession over the years and were current on their payments until they ran out of money in April, 1995. The Friedmans did everything they could to make the business succeed and repay Repossession.

The only representation made by Mr. Friedman which turned out to be false was his statement on April 29, 1995, that he would produce a check on Monday morning to cover the shortfall in the inventory. At this point, the cars and the money were gone. Repossession did not rely on this statement to its detriment.

There was no evidence that the Friedmans made any effort to conceal the sale of cars with deceptive statements prior to April, 1995, when everything collapsed. Indeed, Repossession maintained the official inventory of cars. Every monthly inventory from May, 1994, through March, 1995, checked out with the cars on the lot.

It was only when the inventory was taken on April 29, 1995, that certain differences were discovered.

The Friedmans did not conceal their inability to make their payments pursuant to the Floor Plan Agreement. In fact, they made their payments through March, 1995. When Mr. Friedman tried to explain to Mr. Felder and Mr. Lyons that the business was in trouble, they did not want to hear about it. Repossession cannot stick its head in the sand, and then claim that it was defrauded by the Friedmans.

The Supreme Court's recent decision in Kawaauhau v. Geiger, 523 U.S. 57, 118 S.Ct. 974 (1998) provides the analytical framework for the Court's discussion of the § 523(a)(6) issue. The Supreme Court concluded that "willful and malicious injury" requires a "deliberate and intentional injury." 523 U.S. *at* 61, 118 S.Ct. *at* 977. "Only acts done with the intent to cause injury - and not acts done intentionally - can cause willful and malicious injury." 523 U.S. *at* 61, 118 S.Ct. *at* 977. A deliberate or intentional act that leads to injury is not sufficient to meet the requirement; the debtor must have intended the consequences of the act, not merely the act itself. 523 U.S. *at* 61, 118 S.Ct. *at* 977.

In this proceeding, Repossession argues that the Friedmans' failure to remit proceeds generated from the sale of its collateral constitutes a willful and malicious injury within the meaning of § 523(a)(6). The Friedmans denied any intent to injure Repossession.

The Floor Plan Agreement did not require that the sales proceeds from the cars be segregated into a separate account. All

the funds received from the sale of cars were deposited in an Ideal bank account along with other funds. Ideal was authorized to pay for the vehicles which it sold out of any of its funds. Payments to Repossession came out of the same bank account that Ideal used to pay its other creditors. When the money ran out in April, 1995, Repossession suffered along with Ideal's other creditors.

The evidence in this case clearly demonstrated that it was the Friedmans' intent to keep their business afloat; it was not their intent to harm Repossession or its collateral. In re Crump, 247 B.R. 1, 5 (Bankr. W.D. Ky. 2000); In re Wikel, 229 B.R. 6, 7 (Bankr. N.D. Ohio 1998); In re Tomlinson, 220 B.R. 134, 138 (Bankr. M.D. Fla. 1998). The business was never as profitable as Mr. Lyons promised, and Mr. Lyons' refusal to let Mr. Friedman attend the necessary car auctions doomed the business. Unable to replenish their inventory, the Friedmans were unable to keep customers returning to the lot. As a result, the Friedmans had to use a portion of the proceeds from the sale of the cars to cover the expenses of running the business such as rent, utilities, and salaries. There is no evidence of any funds being used to pay anything other than business expenses.

The Friedmans did not use any of the funds for personal gain. The salaries that they drew from the business were not extravagant. The payments they made in May, 1995, after the business closed were for minimal living expenses. The Friedmans lost their initial investment of $50,000, another $165,000 from operating the business, and their business. The Friedmans did not endure a year of hard work and significant monetary losses just to injure

Repossession and its collateral. They were doing their best to keep the business going.

The totality of the circumstances indicates that the Friedmans used the proceeds from the sale of the cars to keep their business afloat. Their conduct cannot be classified as "willful and malicious" under § 523(a)(6).

For the foregoing reasons, the Plaintiff's Complaint to Determine Dischargeability of Debt is denied.

This Opinion is to serve as Findings of Fact and Conclusions of Law pursuant to Rule 7052 of the Rules of Bankruptcy Procedure.

See written Order.

ENTERED:

_____
LARRY LESSEN
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT

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HOWARD FRIEDMAN and VIVIAN FRIEDMAN,	)	
	)	
Defendants.	)	

O R D E R

For the reasons set forth in an Opinion entered this day,

IT IS HEREBY ORDERED that the Plaintiff's Complaint to Determine Dischargeability of Debt be and is hereby denied.

IT IS FURTHER ORDERED that the debt of Howard and Vivian Friedman to Latin American Casinos, Inc., d/b/a Repossession Auction, Inc. be and is hereby discharged.

ENTERED:

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LARRY LESSEN
UNITED STATES BANKRUPTCY JUDGE